



FINAL REPORT

Electronic Commerce Study Committee

February 2013

MEMBERS:

Senator Matt McCoy,
Co-chairperson
Senator Randy Feenstra
Senator Tom Reilly

Representative Chuck Soderberg,
Co-chairperson
Representative Chris Hall
Representative Thomas R. Sands

Staff Contacts:

Richard Nelson, Senior Legal
Counsel, (515) 242-5822
richard.nelson@legis.iowa.gov

Ann Ver Heul, Senior Legal Counsel,
(515) 281-3837
ann.ver.heul@legis.iowa.gov

Contents:

- I. Proceedings
- II. Internet Sales Taxation—National
Conference of State Legislatures
(NCSL)
- III. Electronic Payment Transaction
Interchange Fees—NCSL
- IV. Iowa Department of Revenue
- V. Iowa Division of Banking
- VI. Office of the Attorney General
- VII. Iowa Bankers Association
- VIII. Community Bankers of Iowa
- IX. Iowa Credit Union League
- X. Panel Presentation—Retail
Community
- XI. Materials Filed With the Legislative
Services Agency

AUTHORIZATION AND APPOINTMENT

The Electronic Commerce Study Committee was authorized by the Legislative Council for one meeting day during the 2012 Legislative Interim. The committee's charge was to collect information from stakeholders relating to the collection of sales and use taxes from local and Internet-based retailers (known as "E-fairness") and the collection of electronic payment transaction interchange fees (known as "swipe fees").



Electronic Commerce Study Committee

I. Proceedings

The committee met on Friday, December 21, 2012, in Room 103 of the State Capitol to hear testimony from various experts and interests. The committee did not make recommendations.

II. Internet Sales Taxation – National Conference of State Legislatures (NCSL)

Mr. Max Behlke, Manager of State-Federal Relations, NCSL, provided an overview of the issue of online sales taxes from both a state and federal perspective. Mr. Behlke cited United States Supreme Court rulings holding that states cannot force out-of-state retailers to collect sales tax owed by consumers for catalog or Internet sales transactions, with the rationale that it would place an undue burden on interstate commerce. He indicated that this puts local businesses at a disadvantage which will only increase with the continued expansion of electronic commerce. He identified and reviewed several options for states seeking to increase electronic commerce sales and use tax revenue, including becoming a member of the Streamlined Sales Tax and Use Agreement, passing an affiliate nexus or “Amazon law,” enacting notice laws that require a remote vendor to provide information about taxes to buyers, urging Congress to pass legislation that would give states remote tax collection authority, and entering into tax collection agreements on an individual basis with specified large-scale, Internet retailers. Mr. Behlke additionally summarized federal legislation designed to confer sales and use tax collection authority on the states, including the Main Street Fairness Act, the Marketplace Equity Act, and the Marketplace Fairness Act. He indicated that sponsors in both chambers of Congress have made the legislation a priority.

III. Electronic Payment Transaction Interchange Fees – NCSL

Ms. Heather Morton, Program Principal, Fiscal Affairs, NCSL, provided a corresponding federal and state overview relating to the issue of electronic payment transaction interchange fees. Ms. Morton described how an interchange fee is deducted and distributed between or among a financial institution issuing a credit card, a merchant’s financial institution, and the credit card network processing a sales transaction. She discussed the impact of Section 1075 of the federal Dodd-Frank Act (the so-called Durbin Amendment) on debit card interchange transaction fees and identified exemptions to the amendment’s provisions (most notably any issuers having assets of less than \$10 billion). Ms. Morton additionally discussed interchange fee legislative activity at the state level, indicating that between 2005 and 2012 a total of 122 bills and resolutions have been introduced addressing one or more issues involving interchange fees. Of this total, she stated that 10 resolutions and three bills have ultimately been enacted. Ms. Morton also identified states which have introduced legislation relating to exempting sales and use taxes from interchange fee calculations, similar to legislation introduced in Iowa during the 2012 Legislative Session.

IV. Iowa Department of Revenue

Ms. Victoria Daniels, Administrator of Tax Policy and Communications, Iowa Department of Revenue (IDR), and Dr. Amy Harris, Manager, Tax Research and Policy Analysis Section, IDR, provided information from the department’s perspective regarding the Internet sales taxation issue. Ms. Daniels reiterated some of the NCSL overview regarding the impact of Supreme Court rulings



on state Internet sales and use tax collection, and clarified and recast figures previously supplied during that overview relative to uncollected use tax from remote sales and streamlined sales tax member state collection totals for the state of Iowa. She indicated that the department supports federal legislative efforts and is working to develop the appropriate infrastructure and coordinate the necessary parties to be involved in implementation in the event the legislation is enacted. Ms. Daniels additionally commented on the significant potential impact of the legislation both from a revenue generation and retailer and consumer education standpoint.

V. Iowa Division of Banking

Mr. James Schipper, Superintendent of Banking, stated that the division has no position as a regulator regarding the legislation introduced during the 2012 Legislative Session exempting sales and use tax from interchange fee calculations. He indicated, however, that the legislation would impose new requirements on banks, that the state of Iowa has approximately 300 state-chartered banks which range in size from small to very small, and that a disproportionate burden is placed on such banks when new regulatory requirements are imposed. He additionally stated that federal preemption of state regulatory requirements is well-established when a new state law or regulation is determined to be more burdensome than a federal standard. This could result, he indicated, in the inapplicability of the legislation to federally chartered banks doing business in the state.

VI. Office of the Attorney General

Mr. Bill Brauch, Director of the Consumer Protection Division, accompanied by Ms. Jessica Whitney, Assistant Attorney General, reiterated Mr. Schipper's comments regarding the likelihood of federal preemption, stating that experience with litigation where similar federal-state regulatory issues have arisen has strongly favored such preemption and that this would result in the legislation being limited to state-chartered institutions.

VII. Iowa Bankers Association

Mr. Steve Rauchenberger, representing the Electronic Payment Coalition, described the complexity and competitiveness of the national payment card system. He indicated that the system is popular with consumers, incorporates consumer safeguards, is heavily scrutinized, and well-regulated on the national level.

Ms. Sharon Presnell, Senior Vice President, Iowa Bankers Association, repeated the assertion that the proposed 2012 Iowa legislation would likely apply strictly to state-chartered banks, and identified several issues which she contended would prove burdensome to such banks, and to retailers and their customers, if the legislation were to be enacted. Specifically, she stated that currently the necessary infrastructure to exempt sales and use taxes from interchange fee calculation does not exist and would have to be created at a high cost to merchants, processors, networks, and financial institutions. Additionally, a financial institution would bear the credit risk for the entire transaction, including the tax portion, merchants would need specialized terminals and software to itemize and communicate segmented data, and consumers could face paying two separate transactions per sale—one for the product or service and another for the tax portion. Ms. Presnell further distributed a schematic regarding how payment card transactions are



processed, the variables underlying the cost to merchants of accepting credit and debit cards, and the benefits derived by them from doing so.

VIII. Community Bankers of Iowa

Mr. Mike Hollinger, President and Chief Executive Officer, Shazam, Inc., identified and described the various parties involved in the operation of the payment card network, and stated that while the network is highly specialized and complex, it has a relatively narrow set of payment processing rules facilitating the network's efficient operation. He agreed with prior presenters that the proposed legislation would be at odds with the national payment card processing system and would require infrastructure to facilitate it, which does not currently exist.

Mr. Don Hole, Executive Vice President and Chief Executive Officer, Community Bankers of Iowa, stated that establishing a precedent of determining payment system costs based upon the type of payment is ill-advised. He emphasized that the payment system is based on universal acceptance, guarantee and settlement without respect to transaction type, and expressed concern that designating that certain types of payments must be handled in a unique way increases costs to the financial institution and consumer, and has the potential to extend to other types of transactions beyond sales tax.

IX. Iowa Credit Union League

Mr. Jeff Russell, The Members Group, cited as concerns posed by the proposed interchange fee legislation expensive implementation costs and significantly increased consumer and retailer confusion regarding separating sales transaction components and interchange fee calculation.

Mr. Justin Hupfer, Vice President of Government Affairs, Iowa Credit Union League, stated that the appropriate venue for any legislation relating to the regulation or calculation of interchange fees is at the federal level, and that the bills which have been proposed evidence Congressional intent to exempt small entities and are focused on debit versus credit card transactions. He additionally noted that interchange fees are in part designed to help cover some of the financial institution's liability for fraudulent credit card transactions, and that excluding a portion of that transaction is inconsistent with how the electronic payment system is designed to operate. He expressed support for legislation introduced in other states establishing standards relating to how long electronic data can be stored following the processing of a sales transaction, and prescribing merchant liability to financial institutions in the event the standards are not abided by.

X. Panel Presentation—Retail Community

Mr. Jim Henter, President, Iowa Retail Federation, characterized interchange fees as a hidden expense negatively impacting consumers and business owners. He estimated that Iowa retailers incurred in excess of \$30 million in interchange fees based on retail sales tax collections of almost \$2 billion in 2011, and suggested that retention of these amounts by retailers would have had a positive economic impact and stimulated job creation. Mr. Henter disputed the contention that an appropriate infrastructure to facilitate implementation of the legislation could not be readily created, and noted that governmental entities have the ability to impose a surcharge to cover electronic payment processing costs, which is not available to retailers.



Mr. Craig Walter, Executive Vice President, Iowa Lodging Association, identified interchange fees as a significant cost of doing business for the lodging industry, which collects both sales and use tax and local option sales taxes for a combined 12 percent tax rate. He echoed Mr. Henter's comments regarding the positive economic impact and business expansion opportunities which would be facilitated by implementation of the legislation.

Mr. Will Rogers, Director of Governmental Affairs, Iowa/Nebraska Farm Equipment Dealers Association, estimated that association members incur a minimum of \$500,000 in interchange fees annually based on sales tax collections, and agreed with the previously expressed support for reinvestment of the money paid in fees in business expansion opportunities.

Ms. Jessica Dunker, President and Chief Executive Officer, Iowa Restaurant Association, characterized her members as not only acting as the state's tax collectors, but also incurring an expense for doing so based on the current interchange fee calculation structure. She estimated that the average restaurant incurs more than \$1,100 in interchange fees charged on sales tax, which could be redirected to cover the cost of food for a full day of operation, new equipment, and employee salaries, and that the cumulative financial impact on Iowa's hospitality industry amounts to nearly \$4 million annually. She stated that enacting the proposed legislation would evidence a significant intent that the state is seeking creative solutions to fuel economic growth and investment in retail businesses.

Mr. Gray Taylor, Executive Director, Petroleum Convenience Alliance for Technology Standards, stated that convenience stores can be characterized in general as selling the most heavily taxed items and that the impact of interchange fee imposition on the sales and use tax portion of their retail sales is in the multiple millions of dollars. Mr. Taylor provided a handout depicting a financial snapshot of the convenience and petroleum store industry, the extent to which it constitutes a key source of tax revenue, and interchange fee cost breakdowns. He said the issue of interchange fee imposition and calculation is not fundamentally a banking issue, but rather determined by Visa and MasterCard.

XI. Materials Filed With the Legislative Services Agency

The materials listed were distributed at or in connection with the meeting and are filed with the Legislative Services Agency. The materials may be accessed from the "Committee Documents" link on the committee's Internet site:

<https://www.legis.iowa.gov/Schedules/committee.aspx?GA=85&CID=850>

1. Tentative Agenda.
2. Electronic Commerce Study Committee.
3. Statement — Petroleum Marketers and Convenience Stores of Iowa (submitted post-meeting).
4. Committee Charge.
5. Committee Member Contact Information.



Electronic Commerce Study Committee

6. Proposed Committee Rules.
7. Online Sales Taxes — National Conference of State Legislatures Presentation.
8. Collection of Iowa Sales and Use Tax From Local and Internet-based Retailers.
9. Interchange Fees — General Information Articles.
10. House Study Bill 666 — Interchange Fee Bill Introduced During the 2012 Legislative Session.
11. Background Information — Legislative Services Agency, Legal Services Division.
12. Interchange Fees — National Conference of State Legislatures Presentation.
13. Interchange/How Payments Work — Iowa Bankers Association.
14. Committee Remarks — Community Bankers of Iowa.
15. How Payments Work — Community Bankers of Iowa.
16. Opposition to State Regulation of Interchange — Iowa Credit Union League.
17. Committee Remarks — Iowa Retail Federation.
18. Interchange Rate Schedule — Iowa Retail Federation.
19. Committee Remarks — Iowa Restaurant Association.
20. Handout — Petroleum Convenience Alliance for Technology Standards.
21. Extending Sales Taxes to Digital Goods and Services — Iowa Department of Revenue (submitted post-meeting).

39421C